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Be Ready: Major Changes Coming to Health Care and Related Taxes in 2013

Health insurance plans purchased on one of the health care exchanges, created by The Affordable Care Act of 2010 (ACA), will be effective January 1, 2014, which is also when federal subsidies to aid in buying health insurance will start and penalties for not purchasing it will be assessed.

The revenue from new taxes and fees will help pay for broadening insurance coverage to about 30 million uninsured Americans in 2014.

However, in many ways the biggest changes brought about by the ACA are happening *this year*. These include: a wide range of tax increases, payment increases for Medicaid doctors, simplified plan language in Summary of Benefit Coverage documents, expanded coverage of Medicare prescription drug plans, and the opening of health care exchanges October 1, 2013.

Below is a summary of what changes to expect this year. Everyone will be affected, from the sole proprietor to the largest corporations, from the uninsured to the fully insured, and from those below the poverty line to top wage earners.

Your Taxes Will Increase and Get More Complex

The Affordable Care Act creates or increases at least five taxes to help finance the law.

1. Payroll Tax: Employers are already required to withhold 7.65 percent of workers' wages to support the elderly and disabled. Old-Age, Survivors and Disability Insurance (OASDI) was established by law in 1965, and is what we now commonly refer to as Medicare. Currently, 1.45 percent of that 7.65 goes toward paying Medicare's hospital bills. Beginning this year, the ACA increases the Medicare hospital tax by 0.9 percent for any individual who earns more than $200,000, or $250,000 for joint tax filers.

   Employers will be able to deduct the extra 0.9 percent tax for individual employees on the portion of income that exceeds $200,000, but the law does not permit them to withhold additional payroll taxes to account for joint tax filers whose combined incomes exceed the limit. This means that

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for the first time some taxpayers will have to calculate and pay a portion of their payroll taxes on their federal tax return.

2. Investment Income Tax: The ACA creates a new 3.8 percent tax on investment income above the same income thresholds listed above, namely $200,000 for individuals and $250,000 for couples filing jointly.

3. Medical Device Tax: A 2.3 percent tax will kick in on the sale of medical devices, including implants and other devices used in a doctor's office or hospital. The tax does not apply to devices sold in retail stores, like glasses and contact lenses.

4. Flexible Spending Account Limits: Contributions to FSAs, which allow people to set aside money tax-free to pay for medical expenses, will be capped at $2,500. The limit will then be increased by an annual cost-of-living adjustment. Previously, there was no mandated cap, but many large employers set a cap of $5,000/year. This change will cause health care spending which was previously a tax deduction, to be paid with after-tax dollars, thus increasing a taxpayer's effective tax rate.

5. Medical Expense Tax Deductions: Before the passage of the ACA, the proportion of certain medical expenses that could be deducted by most tax filers must have exceeded 7.5 percent of adjusted gross income. Starting this year, that amount will increase to 10 percent. This change will reduce people's tax deductions and, like the changes to FSA limits, result in a higher effective tax rate.

6. Employer Tax Subsidy Eliminated: For the tax year that began January 1, 2013, employers participating in the Retiree Drug Subsidy (RDS) program will lose the tax-free status of this federal subsidy, which helps pay for retirees' drug benefits. The RDS program will now be taxed at the corporate level, thus increasing the company's effective tax rate. The move is expected to accelerate a continued decline in the number of employers that offer not only drug benefits but broader health insurance plans to retirees. There is a far superior alternative to the RDS, called the Employer Group Waiver Plan, or "Egg Whip". For more information click here.

A Synopsis of Your Insurance Plan Will Be Available in Simple English

To be clear, the health plan policy will remain a long and complicated document in small font, filled with legalese.

However, for all health plans with open enrollment periods after September 23, 2012 (which includes most plans with an effective date of January 1, 2013), The Affordable Care Act requires insurance companies to send their members a standardized, four-page Summary of Benefit Coverage or “SBC”. This may sound like a good idea but all qualified group employer plans are already required by law to send every plan participant and member a short, easy to understand, plain English summary of the plan’s benefits in the form of a Summary Plan Description or “SPD”. Perhaps the new SBC will be more beneficial to people purchasing individual plans but, if that is the case, it should have only applied to those plans. The vast majority of employers probably find the new SBC requirement duplicative, unnecessary, and inefficient. Ultimately, it will increase the cost of employer health plans.

Expanded Coverage in Medicare Part D Prescription Drug Plans

In 2013 Medicare seniors with a Part D prescription drug plan will pay an annual deductible of $325 and 25 percent of drug costs, up to $2,970. Once their total drug costs reach that amount, some seniors face a coverage gap or so-called “doughnut hole” until total drug costs increase to about $6,773, when catastrophic coverage kicks in.

The gap in Medicare Part D prescription drug coverage will narrow slightly this year and continue to do so until 2020, when Medicare-eligible seniors will pay 25 percent of the cost of both brand-name and generic drugs.

Starting January 1, 2013, Medicare-eligible seniors with a drug-coverage gap will be responsible for a smaller share, paying 47.5 percent of the cost of brand-name drugs and 79 percent of the cost of generics.

As a reference point, in 2012, seniors paid 50 percent of the cost of brand-name drugs and 86 percent for generic medications in the coverage gap.

Primary Care Doctors Seeing Medicaid Patients Will Get a 73 Percent Raise

The federal government wants doctors to continue serving the Medicaid population even though Medicaid pays them significantly less than doctors charge in private practice. The Congressional Budget Office estimates that Medicaid will gain seven million new enrollees in 2014, as a result of the health law expanding the program up to 133 percent of the poverty line. These means lots more patients and fewer doctors willing to take a severe pay cut and treat them.

To fix this sticky problem, the ACA includes a provision that hikes primary-care reimbursements from Medicaid to match those of Medicare for 2013 and 2014. On average, that will mean a 73 percent raise for Medicaid doctors.

The ACA Exchanges Will Open for Business

Even though the policies on the new health care exchanges will take effect January 1, 2014, both state- and federally-operated exchanges must be open and fully operational by October 1 of this year. This deadline was set so people will have enough time to go on the exchanges, review the available plans and make a purchase decision well before next January.

December 14, 2012 was the deadline for each state to notify the Department of Health and Human Services (HHS) if it planned to operate its own exchange or leave it to the federal government; 18 states elected this option and more may do so. That number was higher than expected and will add to the federal government's cost of implementing the ACA. It could also delay the launch of some or all of the exchanges. See related Bloomberg article here.

For more information on the potential pitfalls for exchanges in selling individual policies, please click here.

Some Potentially Good News: Growth in Health Care Cost Expected to Slow

According to actuaries at the Center for Medicare and Medicaid Services (CMS), the United States is projected to spend $2.9 trillion on health care in 2013. That represents a 3.8 percent increase over the $2.8 trillion, which the CMS estimates the government spent for all of calendar 2012.

A 3.8 percent growth rate would be the slowest growth rate in health care spending in decades. It's impossible to determine what impact the ACA will have on health care costs when the act is fully implemented. However, according to the same CMS actuaries, this historic low growth rate, if it actually happens, has mostly to do with slow income growth and very little to do with The Affordable Care Act.

"Consumers are expected to remain sensitive to rising health costs, particularly given continued low projected income growth," they write. "In this environment, consumers are likely to continue to be judicious in their use of health-care services."

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